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FM AMEMBASSY BUDAPEST
TO RUEHC/SECSTATE WASHDC 3102
RUEATRS/DEPT OF TREASURY WASHDC
INFO RUCNMEM/EU MEMBER STATES COLLECTIVE

UNCLAS BUDAPEST 000630

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SIPDIS

STATE FOR EUR/NCE AND EB/IFD, AND INR/EC
TREASURY FOR JEFF BAKER AND LARRY NORTON

E.O. 12958: N/A
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SUBJECT: HUNGARY WINS MERCEDES-BENZ AND EU INNOVATION CENTER

SUMMARY

¶1. (U) Hungary is celebrating its recent selection over other countries in the region for both a new Daimler car plant and the European Institute for Innovation and Technology. The Daimler plant alone is expected to add another 1 to 1.5 percent to Hungary's GDP. In total, some USD 1.7 billion will be invested in Hungary for both projects in the next few years, creating some 2,500 new jobs directly and at least 10,000 jobs indirectly. Both are unexpected) and perhaps undeserved) votes of confidence given the government's record on competitiveness. End Summary.

LUXURY COMES TO HUNGARY

¶2. (U) On June 18, German car company Daimler AG announced that it would invest USD 1.24 billion to build a new plant in the southern Hungarian city of Kecskemet to manufacture its Mercedes-Benz A and B-class vehicles. With expectations that the plant will directly create 2,500 new jobs and a total of 10,000 to 14,000 jobs through local suppliers, media reports predict a 1.0 to 1.5 percent boost to Hungary's GDP. While plant construction is expected to begin next year with an estimated first roll-out in 2011 of 100,000 cars annually, a memorandum of understanding and details to the agreement have yet to be made. EU approval is also needed and expected to take three months. According to media reports and Parliamentary staff, state subsidies amounting to USD 255 million, (the highest allowed by the EU and offered by all other competing countries) will be part of the package. Media reports indicate that USD 191 million of the subsidies will be in cash.

¶3. (U) Former Minister of Economy Janos Koka believes the city's easy access to motorway roads in the region is why it was chosen over the three other competing bids from Romania, Poland, and Serbia. The media also cited labor availability, successful assembly operations by Audi and Suzuki, and the city's long tradition in vocational training as other reasons for its competitive advantage.

HUNGARY SCORES OVER POLAND AGAIN

¶4. (U) On the same day, the EU also announced the selection of Budapest as the location for the European Institute of Innovation and Technology. As the EU's main center for integrating research and development ideas with the business community, it will employ a staff of 50 to 60 people and have a budget of USD 465 million for 2008-2013. The institute, nick-named "Europe's Brain" by one MFA official, will focus first on energy and climate change. According to press reports, Budapest was selected over Wroclaw because Poland already has the EU border agency Frontex while Hungary has yet to be the home of an EU center.

COMMENT: VICTORY OR DISTRACTION?

15. (SBU) While the EU's decision to select Budapest for its innovation center was expected, Hungary's late entry to the competition as well as its high labor costs and unfavorable tax structures make Daimler's choice of Kecskemet a surprise. Although Kecskemet may have indeed been a strategically good choice for Daimler given its location, it has already led several high-ranking officials to rationalize a questionable record on competitiveness. We are concerned that this recent spate of good news may compound the sense of complacency that is leading the GoH to delay much needed structural reforms.

Foley